"Cipla Limited Q2 FY20 Earnings Conference call"

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MODERATOR: **MR. CHIRAG TALATI – KOTAK SECURITIES LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to the Cipla Limited Q2 FY20 Earnings Conference Call hosted by Kotak Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Chirag Talati from Kotak Securities Limited. Thank you and over to you, sir.

Chirag Talati: Hi, good evening, everyone. This is Chirag from Kotak Institutional Equities. I thank the Cipla management team for giving us the opportunity to host this call today. From Cipla we have with us today, Mr. Umang Vohra – MD and Global CEO, Mr. Kedar Upadhye – Global CFO, and Naveen Bansal from the Investor Relations team. Over to you, sir!

Naveen Bansal: Thank you, Chirag. Good evening and a very warm welcome to Cipla's Quarter 2 FY20 earnings call. I am Naveen from the Investor Relations team at Cipla.

Let me draw your attention to the fact that on this call our discussion will include certain forward-looking statements which are predictions, projections or other estimates about future events. These estimates reflect management's current expectation of the future performance of the company. Please note that these estimates involve several risks and uncertainties that could cause our actual results to differ materially from what is expressed or implied. Cipla does not undertake any obligation to publicly update any forward-looking statement whether as a result of new confirmations, future events or otherwise.

I would like to request Kedar to take over.

Kedar Upadhye: Thank you, Naveen and good evening to all of you. Welcome to our Earnings Call for the Second Quarter of Fiscal 2020. I hope you have received the investor presentation that we posted on our website.

This quarter is quite strong for us and stable after a muted quarter one which highlights the inherent strength of our businesses. This quarter has seen significant recovery and stabilization of the distribution model change on the trade generic side, strong growth in the prescription branded business in India with seasonal triggers driving growth in acute therapies as well, continued momentum in the South African private market business, and retention of share in key assets in the US despite multiple competitive entries.

On Cinacalcet, contribution in value terms has substantially normalized in the quarter and it is quite close to measuring at the base levels.

With this comment, let me come to the financials for the quarter:

For the quarter, overall revenue from operations stands at 4,396 crores which recorded a healthy year-on-year growth of 10% with strong performance across our key businesses of India, South Africa and US. I would like to clarify that the numbers for the quarter do not include any significant benefit from the spillover that we had mentioned in the last quarter. For our India business, the net delta in the opening and closing spillover is nil. For emerging markets, it is around only $5 million or so. Gross margin after material cost stood at 67% for the quarter driven by increased share of Indian branded business, South African private business and our limited competition assets in the US. This got partially offset by the increased share of the generics business as compared to the last quarter. Total expenses which include employee costs and other expenses stood at 2,025 crores increased by 7% on a sequential basis. Employee cost for this quarter stood at Rs, 762 crores largely flattish on a sequential basis. Other expenses for this quarter which include R&D, regulatory, quality, manufacturing and sales promotion costs stood at 1,263 crores, an increase 12% on a sequential basis. This increase is driven by growth investments in various part of our business. Total R&D investment for this quarter stood at 7% of revenue or Rs. 295 crores. This includes charges for the ongoing respiratory trials for Advair.

During the quarter, we completed the patient randomization for generic Advair in line with our targets.

EBITDA for the quarter stands at Rs. 909 crores or 21% to sales. Tax charge for the quarter stood at Rs. 201 crores. We are looking at our full year ETR of 29% to 30%. I can explain the details on tax later. But this year, we propose to continue with the old regime of tax rates. Profit after tax stood at Rs. 471 crores or 11% to sales.d

During the quarter, we prepaid loan of USD 110 million which was taken for the InvaGen acquisition almost 1 year in advance considering our cash holdings. Our long-term debt now stands at $440 million which is mainly used to fund the InvaGen acquisition and South African Rand 100 million for Mirren acquisition.

We also have working capital loans which act as natural hedges towards our receivables. Total net debt-to-equity ratio is at 0.08 and continues to be quite healthy. Outstanding forward contracts as a hedge for receivables as of 30th September are USD 235 million and South African Rand 541 million. During the quarter, we have also hedged a certain portion of our forecasted export revenues. The outstanding cash flow as of 30th September are USD 168 million and South African Rand 280 million.

Thank you and I would now like to invite Umang to present the Business and Operational Performance.

Umang Vohra: Thank you, Kedar. We are pleased to report strong recovery across our businesses during the quarter with overall revenues growing 10% on a year-on-year basis. We are focused on continuing the momentum in the coming quarters.

We took certain determined steps to strengthen commercial discipline which has demonstrated resilience and strong fundamentals of our business. Let me start with some of the key highlights for the quarter:

India trade generics:

During the quarter the change in the distribution model implemented in quarter 1 has stabilized and the business has come back strongly, highlighting the strength of our portfolio. The business recorded a quarter-on-quarter growth of over 60% on a reported basis while the order booking was even higher. Our billed numbers for the quarter were nearly the same as previous year. We are focused on continuing the journey in the coming quarters and quarter 3 should see the business growing over the previous year.

On our India branded business – the business delivered strong numbers growing 13% year-on-year basis. We saw robust performance across all our key therapies which outpaced the market significantly.

South Africa – Our business delivered strong performance growing 12% year-on-year in ZAR terms. The private market business recovered strongly growing at 13% in local currency terms during the quarter. As per IQVIA, Cipla continued outperforming the market and grew over 3x the market growth rate at 7%.

On the U.S. generic side – the business delivered 25% growth year-on-year basis to close the quarter at 135 million. We have retained share in Cinacalcet and as Kedar has said, it is Cinacalcet has reduced significantly from quarter 1.

In emerging markets, we strengthened our portfolio offering in focus markets. In Sri Lanka, we entered into a strategic partnership with Novartis for marketing and distribution of the Ultibro Breezhaler. We are pleased to report that we have signed a strategic partnership with Novartis effective October 1st to market the respiratory portfolio in the Australian market. Overall, the revenue is growing 10% year-on-year. We saw EBITDA growing strongly at 21%.

Let me move to the business-wise performance now:

Overall, the India business including the generics and branded came strongly to deliver 29% growth on a quarter-on-quarter basis. This was driven by performance across key therapies and strong seasonal triggers on the branded side and a strong recovery on the generic side highlighting the resilience of the business post the distribution model change in quarter 1. We hope to continue the momentum in the coming quarters and drive growth in the business.

The branded business grew 13% year-on-year driven by performance across both our chronic and acute therapies. Seasonal triggers help the acute business drive over 15% year-on-year growth in primary sales.

On the secondary side, Cipla continued to perform well across key therapeutic areas.

Chronic therapies in India continued to drive a significant share of growth for us and grew 15% as per IQVIA MAT September 2019 versus 12% for the industry.

Amongst our key therapies, in Respiratory Cipla grew by 15% versus the market growth of 10%. In Cardiology, Cipla grew 17% versus the market growth of 12% and in Urology Cipla grew 15 versus the market growth of 14. We continue to maintain our leadership position across Respiratory and Urology. 14 of the top 22 brands of Cipla continued to feature among the top 300 brands in the IPM and have outpaced the industry growth as per IQVIA MAT September 2019.

For the North America business – despite multiple competitors launching the generic product to Sensipar, we retained good market share in Cinacalcet. We have seen fairly aggressive price reduction for the product which was expected. In addition, on an overall basis launches such as Pregabalin have facilitated relatively strong growth of 25% on a year-on-year basis resulting in our numbers growing to 135 million.

During the quarter, we announced the launch of Daptomycin as well. Increasing contribution from new launches has been driving gross margin expansion for the business. During quarter 2, we saw our gross margin expanded by 500 basis on a year-on-year basis.

We are progressing well on our trials for respiratory products. We are currently tracking Albuterol as a launch in the early part of first half of 2021 and our limited competition engine should resume in quarter 4.

In the SAGA region, which includes South Africa, Sub-Saharan Africa and the Cipla Global Access business, our overall South Africa business grew strongly at 12% year-on-year in local currency. The private market business recovered strongly from quarter 1 to drive 13% year-on-year growth. In secondary terms, private market continued the momentum growing over 3x the market at 7% as reported by IQVIA MAT.

With the acquired Mirren portfolio growing strongly, Cipla is the third largest player in the OTC market capturing a market share of 6.8. Outside of South Africa, the Sub-Saharan Africa business grew by 7%, while the CGA business declined due to lumpiness in order flows.

The emerging markets business recorded a strong growth quarter-on-quarter to deliver 64 million and recovered from a muted Q1. Apart from the strategic partnership with Novartis, we are working towards bringing our EM biosimilar franchise to fruition with Pegfilgrastim filed in Malaysia and approval received for clinical trials of Bevacizumab in Algeria.

On the institutional specialty business in the US, we plan to submit the IV Tramadol NDA later in the year via our associate company Avenue Therapeutics. We have resumed supplies of Plazomicin in the market.

On the regulatory front, as we shared in our stock exchange announcement, we had an inspection at our Goa plant which ended with 12 observations. These observations are across our 10 units in Goa and none of them are either repeat or related to data integrity. We are working with the agency to address these and have submitted a comprehensive response to the agency.

To close:

While I am happy with the growth reported across markets, I believe our serviceability in product families could have been better. We are focused on continuing the momentum across the key markets in the coming quarters.

Some of our key priorities are to continue to drive momentum in our India business.

On the branded India business side, the coming quarters we will see the launch of Berok 2.0, Cipla's flagship patient focused initiatives in respiratory amongst other therapy focused initiatives.

In South Africa, we believe our private market portfolio can continue to drive strong growth.

In the U.S. market, we will resume with the limited competition launches in quarter 4 and we will be tracking our respiratory filings closely. We will manage the Sensipar / Cinacalcet product for value and retain a larger share of the market.

We remain focused to maintain the highest standards of quality and compliance across the facilities. We will work with the agency on Goa resolution.

I would like to thank you for your attention and I will request the moderator to open the session for Q&A.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Saion Mukherjee from Nomura. Please go ahead.

Saion Mukherjee: Sir, my first question on domestic market. So, your commentary suggests that it is almost normalized as far as trade generic is concerned, right? From third quarter onwards, it would be pretty much business as normal?

Kedar Upadhye: Yes, Saion.

Saion Mukherjee: And Kedar, you mentioned about the spillover impact being nil, I remember it is around 60 crores last quarter because of floods, etc. So, this would have been booked this quarter? I mean, how is it nil, can you explain that?

Kedar Upadhye: Yes, I think the opening spillover got booked this quarter and there is a closing spillover of an equivalent value. So, the net delta between opening and closing for the quarter, Saion is nil.

Saion Mukherjee: But that was a specific instance of flood, right? I mean, is there any issue that you faced this quarter as well which resulted in.....

Kedar Upadhye: Yes, no issues, I think the pattern of the orders and the dispatches across our depots and across a large number of SKUs that we sell in both prescription and generics business probably I think we should get used to this level of the closing spillovers. So, the net delta between opening and closing for the quarter is nil. Quarter 4, typically in the March this gets adjusted, in quarter 4 spillovers typically is usually quite low. It will be there at these levels.

Saion Mukherjee: And second question on the US, Umang I mean, 135 million you mentioned seems to be pretty much the normal base now. So, what would be the concentration of the top 3 products in our sales now?

Umang Vohra: I think the top 3, in my opinion I do not have the exact number but should be closer to about 25%, 20%-25%. And Saion, I think the 135, just so that we are clear does have Cinacalcet in it as well. But it has now almost reached base levels, there will be possibly a reduction in the next quarter on account of Cinacalcet but we hope not by too much.

Saion Mukherjee: Yes I mean, basically, I am assuming that Cinacalcet is one of the top 3 products. I mean, that would be the right assumption to make, right?

Umang Vohra: That is right.

Saion Mukherjee: And including that you are saying it is 20%-25% of your total sales?

Umang Vohra: I think yes, it might be closer to 30 odd percent that, yes.

Saion Mukherjee: And just one last question Umang, before I join back. When you talk about meaningful or limited competition launches what is the size that is in your mind other than Albuterol, of course which can be big. But in general, what is the kind of opportunity size that you are looking at?

Umang Vohra: So Saion, I would say that anything in today's US environment and considering our size, right, we are not a 200 million US business per quarter today. Considering our size and looking at the market, I think somewhere upwards of the 15 million will qualify as limited competition provided you have a long enough window. Now within this, there will be some assets which will be larger. For example, we have been public about Albuterol earlier but some will be larger. But

I think at a 15 million with a 3-6-month limited competition or being alone in the market is a fairly significant thing for us.

Moderator: Thank you very much. Next question is from the line of Neha Manpuria from JP Morgan Chase & Co. Please go ahead.

Neha Manpuria: First on Albuterol, have we got any query or communication from the FDA? I just wanted to understand if there is any risk of a delay in the timeline you have mentioned?

Umang Vohra: So Neha, the timeline is already modified from our correspondence with the FDA. Earlier we were hoping to have a launch sometime in this quarter. So, the timing is already got modified. The agency is in regular contact with us. We have been receiving queries regarding the product files, etc. But if your question is, have we received the CRL or DRL which is later than that? No, we have not done that as yet**.**

Neha Manpuria: My second question is on the gross margin. Kedar, given quarter-on-quarter, Cinacalcet has seen value erosion and our generic business is normalizing. The margin performance, the gross margin performance seems significantly higher than what we were let us say before even Cinacalcet launch. So, is this a normalized level of gross margin? Or is there any one-off, any other one-off in this number?

Kedar Upadhye: There is no other one-off, Neha. The only thing is as we alluded through there could be a marginal drop in the Cinacalcet level from this quarter to second quarter, I mean this quarter 3. And that would be the only impact, other than that depending upon the mix this would vary.

Neha Manpuria: So, what is the, when we look at the business, let us say 4 to 6 quarters, what is the normalized level of gross margins given US margins are improving with every new launch that we are making?

Kedar Upadhye: Yes across the quarters we have been in the range of 65% to 66%, Neha. And my view is we would be in that level of the base gross margin depending upon the price increase, depending upon the work that we are doing on the costs and portfolio momentum there will be a bias to build on it further. But I would think that probably 65-66 is what we could end up with.

Moderator: Thank you very much. The next question is from the line of Anubhav Agarwal from Credit Suisse. Please go ahead.

Anubhav Agarwal: So my question is on Voltaren Gel, the Diclofenac version. So we have, Cipla has maintained market shares very well despite 3 new entrants coming in. Just wanted to check how is the pricing environment in this product? Has after 3 new guys coming in, has like pricing substantially down. Is it still the largest product for us?

Umang Vohra: Yes it is amongst, I would say, yes. It is a close competitor to the largest product and I think the pricing has come off quite significantly. But we have retained share on it.

Anubhav Agarwal: And Umang, all of that is already reflected in this quarter?

Umang Vohra: Yes, all of that is reflected.

Anubhav Agarwal: And on Cinacalcet, when you say that sales will be marginally lower from here. So, effectively we are saying that 130 kind of plus base at least we can expect from here, assuming no more entry comes in Cinacalcet?

Kedar Upadhye: So Anubhav, we would avoid giving specific numbers. I mean, there will be some minor adjustment from the current levels.

Anubhav Agarwal: And in South Africa, how big is this Mirren one? And what was the base? So let us say, when does it normalize South Africa growth for the Mirren acquisition?

Kedar Upadhye: So, I think this year for the full year, we will have full 12 months reflection for Mirren. But this is cough and cold portfolio, Anubhav in South Africa. So this is, the growth of this portfolio is going to be much higher than the private markets organic portfolio that we have.

Anubhav Agarwal: When you report private market grew at 13% that does not include Mirren. That is separate.

Kedar Upadhye: That includes Mirren actually, that includes Mirren.

Anubhav Agarwal: So, what is the growth excluding Mirren? So, just …

Kedar Upadhye: Mirren, for the full year is not beyond, I mean $15 million or so for the full year. We can consider those numbers on a quarterly basis and then appropriately work out. We do not have numbers handy with me now.

Anubhav Agarwal: So just to Mirren, you mentioned is US $50 million for the year, right?

Kedar Upadhye: 15, not …

Moderator: Thank you very much. Next question is from the line of Nimesh Meheta from Research Delta Advisors. Please go ahead.

Nimish Mehta: Just one question on the Cinacalcet and I see a lot many approvals in that product almost 8-9 approvals. But companies who have launched not more than four to five so any particular reason why people are waiting the launch, some color on that will be helpful.

Umang Vohra: Well I think, Cinacalcet is to some extent it is also for many players it is some kind of a risk launch. So, we would think it is probably because of that. I would imagine that would be one of the considerations.

Nimish Mehta: And if you could tell us the market share that we had in Cinacalcet that would be helpful, thank you.

Kedar Upadhye: Yes, we will take it offline.

Moderator: Thank you very much. Next question is from the line of Nitin Agarwal from IDFC Securities Ltd. Please go ahead.

Nitin Agarwal: Umang, on the US specialty business, how should we see the trajectory for the expense build out as well as the expenses on payouts towards acquisitions?

Umang Vohra: So, I think look, some part of the expenses are beginning to come in our base. For example, in this quarter we have already seen expenses bunching up for the specialty launch. And I think the good thing is that the Plazomicin asset is already launched in the market. This we have already billed a fair number. It is going to take a long time to ramp up because anti-infective take relatively long to ramp up. But having said that it is a commercial asset, it is in the market. We do not have too large a team right now for it. We have got barely about 5 to 7 people who are key account managers selling the product. And closer to the Tramadol approval which we are going to be which our associate company Avenue will be filing hopefully by the end of this year. And closer to that approval which will possibly the next year end or early parts of January we will have a fully staffed specialty organization. So, I think there will be some expenses coming in. But the good news is that if we get Tramadol approval which we are very hopeful of. And we have got Plazomicin we will have 2 commercial assets already ready. So, we are hoping that the time period for this specialty expenditure to result in a sustainable business proposition will not take so long. We will be able to accelerate it.

Nitin Agarwal: And secondly, on if you can just sort of refresh that on from a seasonality perspective, Q3 is a decently strong quarter for us from the India business and does it get really impacted, by the way Q2 has been played out?

Umang Vohra: I think there is a seasonal pattern shift. We have seen that the anti-infective season did pull pretty much into the end of quarter 2. Usually, it is somewhere begins to peter-off in the last month. We think based on what we know now that winter might come a little later. So, I think there will be some pulling and ebbing. So, we do not know if it is going to play out exactly the same way because I think there is roughly about a month, a month or 45 day shift in just the way the monsoons came, the way the anti-infective season ran and the way that the winter is expected to come. So, there will be some of that swing. But yes, materially we do not think quarter 3 will be very different in terms of the structural foundations of the market and the demand compared to quarter 2. Of course, the anti-infective season will wear off. That will definitely happen.

Nitin Agarwal: And lastly, the ARV opportunity in the US where we are partnered. I mean, that is going to be a Q4 opportunity or more like an H1 opportunity for next year?

Kedar Upadhye: Nitin, that is more like API kind of an opportunity not I would say, formulation profit share kind of an opportunity. And it would depend upon the customer's schedule, ordering schedule.

Moderator: Thank you very much. The next question is from the line of Sameer Baisiwala from Morgan Stanley. Please go ahead.

Sameer Baisiwala: So, just starting off on Albuterol Umang, I have been tracking this for the last 2-3 years including Perrigo everyone has been delayed regularly. What is the scientific hurdle? Or what is the key asks from FDA on this product?

Umang Vohra: I think Sameer, there is no new requirement because thankfully for us and for every other player, I think the requirements, the guidance it was not as if we were shooting in the dark. The guidance has been available, right? The FDA has routine questions on some aspects of your study which you have to justify, some aspects of what they are seeing in data. And I think it is part of the thing that every limited competition products such as Albuterol will take 2 years for approval as a minimum. So, considering our filing we are roughly around at 2 year time point right now. And I think we are probably thinking that it will take another 4 to 6 months to come.

Sameer Baisiwala: What is the harder part over here, is it the device? Is it the drug? What really is more difficult aspect here?

Umang Vohra: So, different products with the Albuterol category have different issues. For us, I think what had happened specifically to the Albuterol we are after that the innovator change the device roughly about a year back. In the sense that they inserted a drug indicator they added a drug indicator to the device. And therefore, we had to add some studies to show that the drug indicator behaved the same way as a product without the drug indicator. So, that is the reason we are kind of a little delayed.

Sameer Baisiwala: So, those with ProAir would have a different reason, I guess, etc.

Umang Vohra: Yes, that is right.

Sameer Baisiwala: And second question, you are deep into Advair development. Are you thinking of other DPI products after Advair?

Umang Vohra: Yes, we will be doing it is a reasonable thing, Sameer that we will at least be after 70%-75% of the products in the respiratory space. So yes, we will be after them. We may not be the first to market but we will be after a lot of these products.

Sameer Baisiwala: Anything you can share where is the second product in this queue, when you get plan to take it to clinics, etc.?

Umang Vohra: Well, on the DPI side?

Sameer Baisiwala: Yes.

Umang Vohra: Yes, hopefully by the time we exit the year we should have another clinic started on the DPI, on a DPI product. But we also have 2 MDIs that we are likely to that we either have filed or are likely to file or have a partnership with another company on a fairly significant MDI.

Sameer Baisiwala: And the second DPI I presume is going to be Spiriva, if you can share.

Umang Vohra: No, we are not commenting on that, Sameer.

Sameer Baisiwala: And Umang, just on the thinking of the domestic market, I mean I guess it is easier now to do retrospective analysis. So, over last 12 months or so what made the market go down, the growth rates to mid-single digits? And I guess now it is all back up to early double digits. And what is the outlook over here for the broader market?

Umang Vohra: So, I think Sameer, my belief is that the distribution chain in India is still changing. And I am not talking about the trade generics business. That part is a different set of issues and we have dealt with that. But it is my belief that the amount of change in the distribution side of the business is fairly significant. Between hospital groups who are buying as one, between pharmacies which are beginning to consolidate their buying and becoming supply partners to several independents. I think, there is an aggregation and consolidation thesis which is playing out here. And I think those changes are what are creating these timing mismatches between how companies are seeing the business and outside because I would like to believe that core volume growth is still there in the market. And it is coming at a respectable growth rate. So, I think it is probably because of the fact that we are in a cycle where the distribution systems in India are changing. And all of us, Cipla included have to respond to this. And so, the traditional stockist retailer model is probably going through tweaks and edits right now.

Sameer Baisiwala: And is it a good thing for manufacturers that the buyers are getting consolidated or otherwise? And second, what role is GST playing in the whole distribution system?

Umang Vohra: GST's role is clear. I think that is easier to answer. GST is basically taken out a lot of the unorganized market, for sure. We because of the GST and the related impact, I think the cash cycle became fairly stressed in parts of India for the distributors and the current credit environment has also not helped significantly. So, lot of the distribution players who had velocity in their business because of them being able to have a better cash conversion cycle have taken a hit. That is also impacted the pharma billing because remember pharma payables in India are largely within the 21 day period. So, if the cash velocity does not increase it impacts. So, GST is clear. I think the impact was obviously on a large number of players exiting, large number of distributors and players possibly not being as interested in the market. And I think that the other actions have been around liquidity. So, I think that impact on the GST side is clear. I am sorry, what was the first part? I missed.

Sameer Baisiwala: The fact that the distribution systems were undergoing change. So, is it good for manufacturers or not that the customer is consolidating?

Umang Vohra: So, any consolidation obviously, shifts buying power a bit, right? But so, I think from a manufacturing perspective because it is still at a stage where it may not be more than 10%-15% of the market. It is not showing up but obviously, when the shift begins to happen there is a reasonable expectation that the buyers would be a little bit more stronger in terms of negotiating.

Sameer Baisiwala: And just to complete this point, Umang and then I am done. On the GST side, has there been any change in terms of not the distributors but from the freight point of view from the transfer of goods, movement of goods, etc.?

Umang Vohra: Not really, it is become easier and so, what has happened Sameer, is that today a person sitting in Chennai can fulfil an order in Delhi. So, the friction costs are completely removed across both Rx and Gx business. So, it is become easier now for people to do which is why the distribution model is changing because now it is not really about a distributor in Delhi who can supply a retailer in Delhi a guy in Chennai can do it as well.

Moderator: Thank you very much. Next question is from the line of Krishnendu Saha from Quantum Mutual Fund. Please go ahead.

Krishnendu Saha: The Goa plant which we have observation from to declare observation. So, like I am just wondering what is the filing there? What is the awaiting approval? And what is the run rate from that, current run rate from that plant?

Kedar Upadhye: Krishnendu, I think we had clarified that the pipeline from Goa in the next 12 to 18 months is not as high. Some of our, I mean incremental filings especially Respiratory from Indore and in terms of what we are supplying and in terms of what we were able to do in terms of site change and transfer not more than 2.5% of company revenues have single source products from Goa.

Krishnendu Saha: 2.5% you are saying right now?

Kedar Upadhye: Only revenues. That is true. That is right.

Krishnendu Saha: And we still stick the plan that ZEMDRI and Tramadol will be launching together or will be having some will be probably launching ZEMDRI before?

Kedar Upadhye: Yes, Krishnendu, commercial invoicing for ZEMDRI has begun in US. The invoice was rolled out, the product is available in select outlets and we will continue to commercialize it.

Krishnendu Saha: So, we have a sales force right now which is up and running?

Umang Vohra: Yes, we have a key account management.

Kedar Upadhye: We have key account management not really the detailing force.

Krishnendu Saha: And sir last on the Goa thing, what is the status of plant, right now?

Kedar Upadhye: We do not know the status yet. We are working with the agency to get the status. It will take some time.

Moderator: Thank you very much. Next question is from the line of Aditya Khemka from DSP Mutual Fund. Please go ahead.

Aditya Khemka: Just to sort of follow-up on a couple of clarifications. So, Umang, you said that the working capital of distributors has suddenly gone up and there is a liquidity situation. But my understanding was with the implementation of GST the working capital days of distributors are actually come down especially in the branded generic business. Could you clarify on that?

Umang Vohra: Yes, let me clarify. I mean, I mentioned that the earlier conversation with Sameer what I was trying to say was that there are fundamental changes in the distribution side of the business. You have to understand that this business has 21 days of credit between company and the distributors there has barely 20-21 days of credit. And in some parts of the country, it is less than 10 and close to between 10 to 14 depending on whether you are metro or upcountry. For this business to run and because the cycle is 21 days there is an expectation from the distributor when he is selling it to the super stockist or to the retailer that his money also will come back in the same amount of time, right. So, as a result of this, as a result of the fact that there is a credit, there was a credit squeeze in the market which most segments are reporting including auto and everything else. As a result of the fact that a large share of the distribution trade changed after GST there was a shortage of this capital which resulted in the velocity of their business decreasing. Their natural response, so therefore to reduce inventories, right. Because the friction costs also had reduced which is what you are alluding to that are they might have improved their working capital cycle. This impact came on the companies. When distributors reduce their inventory, when their cash cycle in terms of their payments, etc. got delayed. It would have resulted in most companies showing a little bit of sluggishness in growth.

Aditya Khemka: So actually, so I misconstrued your earlier comment, my fault. So, the second question, I wanted to check with you was on the consolidation of buyers comment. So, obviously, I understand the economics of having buyer groups and then having more volume and more bargaining power. But is not it correct that the margins in India are actually regulated, so even if they are buyer groups you can only sell it as 30% discount to the MRP because that is the amount of margin you are supposed to put on or are you envisaging that 3 years-4 years-5 years down the road once they become too large. They will actually be able to bargain with you on that 30% margin and maybe ask for 40%-45% and you would be legally allowed to get that?

Umang Vohra: No, I think what we are trying, to some extent, I think has buying power increases, obviously the buyers become are able to negotiate more. So, I do not know whether this will happen in 3

years or 5 years. But it is a trend that we need to watch. There is no panic on it right now. Nothing is changing in this year or the year after that. A part of our portfolio has this and for all pharma companies, not just us. This is a structural nature of the market that margins are capped for part of the portfolio. And for part of the portfolio which are not controlled the margins are effectively practice not necessarily capped, right. So, I think there is a little bit of a change. But at the same time the government is also trying to expand the list of what they constitute as medicines, etc. So, there are multiple shifts happening in the market and I think one has to just be watchful of this. Aggregation of buying power does increase pressure. It will create more power with people to negotiate better things but nothing is changing overnight in the next, I think at least the 2 to 3 years.

Moderator: Thank you very much. Next question is from the line of Harith Ahmed from Spark Capital. Please go ahead.

Harith Ahmed: Couple of quarters back, I think you had guided for 2 inhaler filings this year one of them, obviously being generic Advair. Would you still stick to that guidance? Are you on track?

Kedar Upadhye: Yes, we are on track. So, the statement was with respect to the filing of 2 inhalers. So, I think for Advair as we told, the randomization of our targeted population is done. Before the end of the year we hope to get to full analysis. And...

Umang Vohra: Early part of next year

Kedar Upadhye: Yes, early part of next year, the filing will happen.

Harith Ahmed: And the second inhaler product has the filings already been done?

Umang Vohra: It is likely to happen by the end of the year.

Harith Ahmed: And my second question is around your comment related to the gross margins where you said we have seen around 500 basis points improvement in our US gross margins. So, would this improvement be materially different if we exclude Cinacalcet?

Kedar Upadhye: Yes, so what I said is over I think last 6 to 8 quarters and in our view in the balance few, coming few quarters as well, I think the base gross margin range for us given the mix of businesses, mix of products, currency, costs it is likely to be between 65% to 66%.

Harith Ahmed: I was referring to the US gross margins. I think, you made a comment that you have seen a 500 basis points Y-o-Y improvement there.

Kedar Upadhye: Yes, so I think to some extent this is attributable to Cinacalcet. And actually the launches that we are making organically in the DTM segment every single launch is beyond 70%-75% gross margin as well. So, directionally every new launch enhances the margin profile. So, I would not

get to specific numbers. But I think in Cinacalcet as well gross margins for the US business have been improving for the last several quarters.

Harith Ahmed: And last one from my side. The intangible assets under development you have around 450 crores and then that is increased by roughly 100 crores in the first half. So, what is this increase on account of?

Kedar Upadhye: See there is a deal that we did with a company to develop inhaled Itraconazole. We publicly announced it in the specialty side. But the initial upfront money paid to acquire the rights of the intellectual property are being captured in that row.

Moderator: Thank you very much. Next question is from the line of Shyam Srinivasan from Goldman Sachs. Please go ahead.

Shyam Srinivasan: Just first one on, I think Kedar's point at the start when you said about the tax rates and why we will continue in the same regime this fiscal. Can you just add some color, Kedar?

Kedar Upadhye: Yes, see our MAT balances are high enough for us. And to avoid a write-off we would this year continue with the existing regime. That way we will save cash taxes. While the reported ETR in the P&L continues at earlier level the cash taxes will be lower.

Shyam Srinivasan: So what are these, what is the level of the MAT balances now? What do we have?

Kedar Upadhye: MAT balances in the balance sheet are roughly around little less than 250 crores or so. So, this year, for the full year we would utilize it fully and from the next year our proposal is to switch it to the newer regime.

Shyam Srinivasan: Yes, so Kedar, you think next year can be like whatever 25% or 26% something like that can happen next year?

Kedar Upadhye: We would have our thoughts crystallized probably towards the end of this year. But directionally, I expect a 200 basis point improvement in the ETR. It could be more also but at this stage, we believe at least a 200 basis point improvement in ETR is possible.

Shyam Srinivasan: And my second question is on the ...

Kedar Upadhye: No, this is for the standalone.

Shyam Srinivasan: Second question is on the tender business. I do not think you got any color on what is happening there, if you can share something on the tender business in Africa?

Kedar Upadhye: See, there is a 3 year period for resetting the prices that resetting has happened. What we are happy is we have been able to retain our volume share in the tender. And in fact, volumes are potentially higher than what they were in the previous cycle. So, we would continue to live in

that regime. And I think there is a change in the product family the Tenofovir combination would shift to Dolutegravir combination gradually. That will help us on the margin side.

Shyam Srinivasan: Kedar but on the pricing, is there any upcoming tender say in January, February whatever, is there something coming up?

Kedar Upadhye: No, I think the last tender has been done for the next 3 years that has been announced.

Shyam Srinivasan: So, nothing will change in the pricing front. It is just now a realization of the volumes that will come through.

Kedar Upadhye: That is correct.

Moderator: Thank you very much. Next question is from the line of Charulata Gaidhani from Dalal & Broacha Stock Broking Pvt. Ltd. Please go ahead.

Charulata Gaidhani: My first question pertains to the new launches in the US? And second, I wanted you to throw some light on the H.R. 4378 regarding withdrawal of authorized generics. Do you expect to see more withdrawals going forward?

Umang Vohra: Yes Charulata, with respect to your first question on the new launches this quarter has seen the benefit of Pregabalin. This is from the InvaGen basket. I mean, that is the one which is notable for the quarter. We are hopeful that if not Q3 at least Q4 will see upcoming launches. The contribution from what we have launched in the last 4 quarters in this quarter's numbers that continues to be quite attractive. Cinacalcet is the prominent one from that and as the pipeline unlocks Q1 onwards of next year, we will see the contribution from new launches in the US as well. We will get back on your second question offline, Charulata.

Moderator: Thank you very much. Next question is from the line of Bharat Seth from Quest Investment Advisors Pvt. Ltd. Please go ahead.

Bharat Seth: Umang, in last quarter we said that we could not, I mean go ahead with the competitive launches due to some capacity constraints. So, how do we see that, I mean is playing out now?

Umang Vohra: No, I think the comment we had made last time was more around our hormonal sterile products, right. And we had said that they were capacity constraints and the capacity issues because of which we could not do. So, we have made taken some measures but those products are still not in our numbers. So, whatever we get from that will be over and above this and it is likely that we will take about 4 to 6 months to get those numbers in.

Bharat Seth: And second thing, I mean we have several plants in India and we were looking for some kind of a consolidation to bring the efficiency. So, what is, I mean our strategy going ahead to bring down or becoming a more cost competitive?

Kedar Upadhye: Yes, Bharat Ji, there is an opportunity, there is a potential opportunity to consolidate volumes across plants that do sort of network assign each plant to a particular region. We are examining what could be that opportunity and what could be the potential rollout plan for it. When it gets crystallized, we will communicate.

Bharat Seth: And Kedar, last question, I mean on, we have invested around 1,150 crores within subsidiary, of course 350 Cipla Health Care remaining is on what account?

Kedar Upadhye: Bharat Ji that is the repayment of the loan that we have made. So, we have repaid our acquisition related loan 1 year in advance. That is about 800 crores or so. Yes and the balance is the acquisition of the state from Fidelity in our Consumer Health JV.

Bharat Seth: And can you give some color on now where do the Cipla Healthcare, I mean and when we were looking for some of them in transferring a generic product also to OTC. So, how the things are moving?

Kedar Upadhye: So Bharat Ji, I think I will not cite any specifics at this point of time. This business is growing very fast year-on-year as we have been communicating. It almost doubled year-on-year for the last 3 years. And this year it will grow in excess of 30% to 35% or so. So, pretty well positioned considering the consumerization potential in India.

Moderator: Thank you very much. Next question is from the line of Damyanti Kirai from HSBC. Please go ahead.

Damyanti Kirai: My question is regarding one comment I think, which we made a few quarters back that you do facility upgradation. We have seen some supply disruption to various markets. So, has that situation normalized now especially for market like US?

Kedar Upadhye: Yes Damyanti, I think that some of the specific situations with respect to capacity augmentations those have been addressed and we will have to be on this journey. It is frankly, it is a journey, automation, digital technologies and manufacturing, some of the remediation related items I think it will be an ongoing journey. Some of the specific actions items that we are refer to have been addressed. In case of many products for the US the benefit of the augmentation has also been realized. So, some of the high margin revenues that we are seeing in US for products like Diclofenac gel or Budesonide is a result of these augmentation efforts that we undertook for the last 1 year.

Damyanti Kirai: So, you are seeing some specific issues already resolved but it is ongoing process to what you say, debottleneck and improve the capacity available, right?

Kedar Upadhye: That is true, Damyanti.

Damyanti Kirai: And also again coming back to I think, one of the previous comments which Umang made that our aim is to launch one complexe generic product every quarter. Are we sticking to that statement?

Umang Vohra: From quarter 4, we are looking at it coming in, from quarter 4 of this financial year.

Damyanti Kirai: So, at least one launch we should be expecting per quarter. That is what you are saying, starting from 4Q.

Umang Vohra: Yes, sometimes they get bunched because we cannot predict the timing. But sometimes we might have 2, sometimes we will not. For example, last two quarters we have not had any because the quarters before that had two, sometimes two per quarter.

Moderator: Sure, the next question is from the line of Vishal Manchanda from Nirmal Bang Securities Pvt. Ltd. Please go ahead.

Vishal Manchanda: I have a question pertaining the albuterol inhaler. Could you guide on what percentage of the US prescription volumes are written by the generic name of Albuterol?

Umang Vohra: Right now, it is a belief that it is upwards of 40%-50%. That is our belief right now.

Vishal Manchanda: So, does that mean these generic prescriptions can be replaced by any of the brand ProAir, Ventolin and even if Cipla gets an approval for, it can be replaced with the same product?

Kedar Upadhye: Vishal, we will have to test this hypothesis as we launch the market.

Umang Vohra: But if it is written as Albuterol, yes, that should be the case. But we have to test this hypothesis.

Vishal Manchanda: And one more, so the innovator having introduced the dose counter in their product. So, would that impact your AB rating on Proventil?

Umang Vohra: No, it will not because we will also be filing our dose counter. We have already filed our dose counter application as well. So, it will not. It will be AB-rated.

Vishal Manchanda: So but would they be having a patent on the dose counter? And would that be subject of litigation?

Umang Vohra: No, there is none. There is no patent on the dose counter. It is widely available dose counter.

Vishal Manchanda: And one more related to the tender business. Is the tender business largely ARV? Or there is also something else to the tender business?

Kedar Upadhye: About 80%-85% is ARV in South Africa balance is across all other therapies split.

Vishal Manchanda: And on the ARV side, do we have an approval for the DLT fixed-dose combination? Or is that awaited?

Kedar Upadhye: We do not have an approval now. We are in the process of seeking the approval.

Vishal Manchanda: Any timelines on when we can get that?

Kedar Upadhye: Would not comment now, Vishal, will revert in the subsequent calls.

Moderator: Thank you very much. Ladies and gentlemen, that was the last question for today. I will now hand the conference over to the management for closing comments.

Naveen Bansal: Thank you everyone for joining us on the call today. In case you have any follow-on questions, you may reach out to myself or write to us at investor.relations@cipla.com. Thank you so much. Have a very good evening.

Moderator: Thank you very much. On behalf of Kotak Securities Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.